

## Message Text

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DRAFTED BY: S/S-O:JHOGANSON

APPROVED BY: S/S-O:JHOGANSON

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FM SECSTATE WASHDC

TO USDEL SECRETARY IMMEDIATE

S E C R E T STATE 207021 TOSEC 100330

NODIS

CHEROKEE

E.O. 11652: GDS

TAGS: ENRG, IR

SUBJECT: ACTION AGREEMENT U.S.-TRAN BILATERAL AGREEMENT

(S/S 7517189)

REF: (A) SECTO 10137) (B) TOSEC 100200, JIDDA 6009

FOR SECRETARY FROM UNDER SECRETARY ROBINSON

1. I CONVEYED TO ANSARY OUR POSITION PER REFS A AND B.  
..... HE REPORTED TO SHAH AND THEN RESPONDED THAT  
IN VIEW OF OUR REQUIREMENT TO GO TO CONGRESS (NOT  
ANTICIPATED AT TIME OF JUNE 30 AND CANNES UNDERSTANDINGS)  
IRAN COULD PROCEED NOW WITH AGREEMENT BASED ON PRESENT  
PRICES ONLY IF USG AGREED TO BACKDATE AGREEMENT TO MAY  
OR JUNE, STARTING INDEXING FORMULA THEN, SO THAT INDEXED  
PRICE RISE BEGINS WITH FIRST OIL DELIVERIES IN  
SEPTEMBER. INTEREST-FREE FEATURE OF US NOTES WOULD  
PARTIALLY OFFSET INDEXING ON SEPTEMBER DELIVERIES SO  
THAT WE WOULD HAVE SLIGHT PRICE DISCOUNT THEN. PRICE  
BREAK PRESUMABLY WOULD WIDEN IN OCTOBER IF OPEC'S  
NEW PRICE SCALE WENT INTO EFFECT.

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2. WHEN I DISCOURAGED IDEA OF OUR BACKDATING AGREEMENT TO THIS EXTENT, ANSARY RETURNED TO SHAH'S EARLIER OFFER OF A FOUR-MONTH FIXED PRICE DEAL AT PRESENT PRICES. SPEAKING PERSONALLY, HE IMPLIED AT ONE POINT THAT GOI MIGHT WEAKEN THIS SHORT-TERM DEAL WITH AN EXPLICIT USG COMMITMENT TO NEGOTIATE AFTER OCTOBER 1 A LONG-TERM AGREEMENT INDEXING PRICES TO NEW OPEC PRICE BASE. IF HE COULD, INDEED, GET SHAH'S AGREEMENT TO DECOUPLE FOUR-MONTH DEAL FROM LONG-TERM COMMITMENT IN PRINCIPLE TO INDEXING ON UNKNOWN NEW OPEC LEVEL, IT WOULD REMOVE OUR MAIN OBJECTION TO SHAH'S COUNTERPROPOSAL. IT WOULD GIVE US 60 MILLION BARRELS AT SUBSTANTIAL PRICE CUT, ASSUMING OPEC RAISES PRICES SUBSTANTIALLY OCTOBER 1, AND IT WOULD PUT IRAN IN VIOLATION OF TWO OPEC RULES WITHOUT DEFENSE THAT IT HAD BOUGHT US AGREEMENT IN PRINCIPLE TO INDEXING AFTER DECEMBER.

3. THUS WE APPEAR TO HAVE THREE OPTIONAL COUNTERPROPOSALS:

(A) SEEK TO CONCLUDE QUICKLY FIVE-YEAR AGREEMENT STARTING WITH NO EARLIER THAN "JULY OIL" FOR DELIVERY IN SEPTEMBER AT PRESENT PRICE PLUS ADJUSTMENT FOR AUGUST U.S. WHOLESALE PRICE INCREASE MINUS NET VALUE OF 120-DAY NOTE INTEREST MORATORIUM; THIS AGREEMENT WOULD BEGIN WITH FOUR-MONTH PERIOD OF USG AGENCY SALES FOR GOI WITHOUT RISK OF USG FINANCIAL LOSS AND THEREFORE NOT REQUIRE CONGRESSIONAL ACTION; WE WOULD IMMEDIATELY SEEK CONGRESSIONAL SUPPORT FOR LONG-TERM PORTION OF AGREEMENT, WITH INDEXING BASED ON JULY PRICES, UNDER WHICH USG WOULD HAVE FIRM COMMITMENT TO TAKE OIL AND CONSEQUENTLY HYPOTHETICAL RISK OF FINANCIAL LOSS REQUIRING APPROPRIATIONS.

(B) SEEK TO CONCLUDE FOUR-MONTH AGREEMENT AT FIXED PRESENT PRICES MINUS VALUE OF SHORTENED INTEREST-MORATORIUM, EFFECTIVE WITH SEPTEMBER DELIVERIES, WITHOUT FIRM COMMITMENT BY EITHER PARTY TO NEGOTIATE LONG-TERM INDEXED AGREEMENT; ANNOUNCE THIS AS PRIMARILY SPECIAL PRICE PROCUREMENT FOR USG DEFENSE AND OTHER SECURITY

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PURPOSRS VUT WITH UFORPETROLEUM PRODUCTS AND WITH RIGHT SWAP IRANIAN CRUDE FOR PETROLEUM PRODUCTS AND WITH RIGHT TO RETURN TO GOI ANY UNUSED BALANCES OF OIL CONTRACTS AT END OF FOUR-MONTHS.

N

(C) DEFER ANY FURTHER NEGOTIATION UNTIL AFTER OPEC PRICE DECISION IS MADE AND IEA HAS CONSIDERED SITUATION.

4. I HAVE IMPRESSION ANSARY IS SO EAGER TO OBTAIN IMMEDIATE INCREASE IN OIL PRODUCTION AND EARNINGS THAT HE WOULD SEEK SHAH'S AGREEMENT TO THE CONDITIONS WE REQUIRE TO MAKE THE SHORT-TERM DEAL ATTRACTIVE, AS OUTLINED IN OPTION B ABOVE. HOWEVER, I HAVE NOT TESTED THIS ASSUMPTION IN DISCUSSIONS WITH HIM. GOI UNDOUBTEDLY WOULD RESIST SOME OF OUR CONDITIONS, PARTICULARLY USG FREEDOM TO AUCTION OR SWAP IRANIAN OIL TO ANY BUYER, AS THIS WOULD CUT INTO IRAN'S REGULAR FULL-PRICE MARKETS THEREBY REDUCING IRAN'S INCREMENTAL EARNINGS FROM DEAL.

5. SHORT-TERM EXECUTIVE AGREEMENT UNDER OPTION B ENTAILS FEWER RISKS OF ANTAGONIZING IEA MEMBERS OR RAISING CONTENTIOUS CONGRESSIONAL ISSUES THAN WOULD OPTION A. IT WOULD NOT BE DEPENDENT ON CONGRESSIONAL ACTION. IT WOULD ACHIEVE BREAK IN OPEC FRONT BEFORE SEPTEMBER 24 OPEC MEETING. IT WOULD GIVE USG SUBSTANTIAL FISCAL BENEFIT -- AT LEAST \$60 MILLION ASSUMING OPEC RAISES PRICE \$1 PER BARREL OCTOBER 1. IT DOES NOT, OF COURSE, NAIL DOWN PRICE BREAK FOR FIVE-YEAR PERIOD AHEAD WHEN OIL MARKET MAY AGAIN BECOME SELLERS' MARKET.

6. IN VIEW OF AKINS' REPORT REF C OF YAMANI'S DECLARED STAND AGAINST ANY OPEC PRICE INCREASE AND YAMANI'S CURRENT DEBATE ON THIS IN TEHRAN, I BELIEVE WE SHOULD NOT RUSH INTO SPECIAL DEAL WITH IRAN PREDICATED ON ASSUMPTION THAT OPEC WILL SUBSTANTIALLY RAISE PRICE SEPTEMBER 24. SAUDI ARABIA'S THREAT TO GO IT ALONE WEAKENS IRAN'S BARGAINING POSITION WITH US AND INTENSIFIES IRAN'S NEED TO FIND WAY TO INCREASE PRODUCTION AND EARNINGS.

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7. ZARB CONTINUES TO OPPOSE SHORT-TERM DEAL (IRRESPECTIVE OF OUTCOME OF CURRENT IRANIAN-SAUDI DEBATE) BECAUSE HE BELIEVES THAT ONLY LONG-TERM ASSURANCE OF MAJOR US BENEFITS IS WORTH THE RISKS HE SEES OF REVIVING CONGRESSIONAL ENTHUSIASM FOR PUTTING USG INTO OIL-IMPORTING BUSINESS. GREENSPAN CONCURS WITH ZARB.

8. RECOMMENDATION: WE RECOMMEND DEFFERAL OF FURTHER DISCUSSION WITH ANSARY ON THIS MATTER UNTIL OUTCOME OF IRANIAN-SAUDI DEBATE IN TEHRAN CAN BE LEARNED.

APPROVE .....

DISAPPROVE .....

RESPONSE SHOULD BE SLUGGED FOR S/S, S AND E ONLY. INGERSOLL

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NNN

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